CAPITAL PROJECTS AND BOND OVERSIGHT COMMITTEE

November 20, 2007

The Capital Projects and Bond Oversight Committee met on Tuesday, November 20, 2007, at 1:00 PM, in Room 169 of the Capitol Annex. Representative Mike Denham, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Representative Mike Denham, Co-Chair; Senator Elizabeth Tori, Co-Chair; Senators Tom Buford, Jerry Rhoads, and Dan Seum; and Representatives Robert Damron, Steven Rudy, and Jim Wayne.

Guests testifying before the Committee: Mitchell Payne and Terri Rutledge, University of Louisville; John Hicks, Governor's Office for Policy and Management; Jim Abbott and Nancy Brownlee, Finance and Administration Cabinet; Dr. Barbara Veazey, West Kentucky Community and Technical College; Gary Cloyd, Kentucky Community and Technical College System; Charles Flynn, Department of Military Affairs; Sandy Williams, Kentucky Infrastructure Authority; Terri Fugate and Tom Howard, Office of Financial Management; Rick McQuady, Kentucky Housing Corporation; Jim Host, Louisville Arena Authority; and Tom Rousakis, Goldman Sachs.

LRC Staff: Nancy Osborne, Pat Ingram, Shawn Bowen, Kristi Culpepper, and Lesa Prewitt.

Representative Denham thanked everyone for the wishes for his speedy recovery and wished everyone a Happy Thanksgiving.

Senator Buford made a motion to approve the minutes of the October 16, 2007, meeting. The motion was seconded by Representative Wayne and approved by voice vote.

Representative Denham asked Nancy Osborne, Committee Staff Administrator, to review the correspondence and information items. Ms. Osborne said the first item of correspondence was from the Council on Postsecondary Education (CPE) reporting its approval of the University of Kentucky's project modification for the Fume Hoods-TH Morgan Building project. She noted the Committee approved the project last month contingent upon CPE's approval.

The second item was from the Governor's Office for Policy and Management (GOPM) reporting on research regarding the sale of naming rights for state-owned facilities. At the Committee's July meeting, questions were raised as to whether there should be a state policy on the sale of naming rights for state-owned facilities when the state awarded a contract to the Bonham Group of Colorado to establish naming rights values for the New Indoor Arena at the Kentucky Horse Park. The correspondence reported no stated limitations were found in the statutes to the sale of naming rights. As part of the inquiry, a letter was sent to the Ethics Commission for guidance on any ethical considerations that should be taken into account regarding this issue.

Representative Wayne suggested that the Committee be kept updated on any developments regarding this issue.

The next item of correspondence communicated revised allocations from the $60 million Department of Parks Development Pool, which updated the December 2006 report to the Committee. It was noted that the $15.2 million in allocations for infrastructure-related developments associated with proposed private development at state parks have been deleted and those moneys have been re-allocated.

Ms. Osborne then briefly reviewed various items in the monthly Staff Update, such as groundbreaking ceremonies for Eastern Kentucky University's (EKU) new Manchester Postsecondary Education Center and a dedication ceremony by the Kentucky Fair and Exposition Center for its new North Wing. She then discussed a temporary injunction issued on October 30, 2007, by the Franklin County Circuit Court relating to whether the state's prevailing wage laws apply to private construction of capital projects on state property.

Ms. Osborne said last month the Committee approved an economic development bond (EDB) grant of $750,000 to the Louisville/Jefferson County Metro Government for the benefit of BAE Systems Land and Armament LP. After the grant was approved, staff became aware of newspaper articles related to an on-going federal criminal investigation and an audit of the company.

When contacted, a Cabinet for Economic Development representative stated they were aware of the federal investigation but that no criminal activity has been proved nor were any allegations specific to any Kentucky operations. Therefore, the federal investigation did not change the status of the EDB grant process. The Cabinet also provided Committee staff with examples of language typically included in the EDB agreements to assure that the project is not jeopardized by any illegal actions of the company.

Representative Wayne said he was upset after reading about the investigation of BAE in the public media, and even more upset that the Committee did not receive information of the criminal investigation and the audit before being asked to approve the award of an EDB grant to this company. He said the Committee needs to be wellinformed and, if such information had been disclosed, the Committee might have hesitated before approving the grant.

Representative Denham next asked Mitchell Payne, Associate Vice-President for Business Affairs and Terri Rutledge, Assistant Vice-President for Business Affairs, University of Louisville (UL), to discuss the Louisville Scholar House project. This project will entail a 50-year land lease of 1.1 acres on UL's Belknap Campus for development of a 56-bed apartment complex including a child development center with a capacity for 186 children. The tenant is the Louisville Scholar House, LLC.

Mr. Payne said this project is funded under the Kentucky Housing Corporations' Scholar House program and is one of five projects statewide. Financing is through federal tax credits and as such, the state's prevailing wage law will apply. The Scholar House is a housing and education program designed to work with both unemployed and under-employed parents so they can become self-sufficient and pursue an education. Participants of the program will receive job training, parental skills, and vocational education skills.

Mr. Payne said an integral part of the program is the child development center. The center will be run by Project Women, Inc., a non-profit entity that owns a portion of the site and is primarily responsible for the overall programming of the Scholar House project. A minimum of 56 of the slots in the center will be reserved for residents, with the rest available to the public. It is expected that the majority of the public slots will be taken by children of the facility and staff of the University.

Mr. Payne said the project has a $12.2 million scope of which $4.2 million is private donations. Private funds have been secured by the University in the amount of $1.5 million for support of the child development center.

Senator Buford said this program has been successful at the University of Kentucky and has helped people that would not have otherwise had a chance at achieving their education or succeeding in life.

Senator Seum asked if the University of Louisville had an option to contract out the management versus operating the facility themselves. Mr. Payne said at this time, the final decision had not been made on management of the facility. Senator Seum asked how this decision would be made. Ms. Rutledge said if the University did decide to outsource the management, it would be a bid process.

In response to another question from Senator Seum, Mr. Payne said the program is open to all parents, including males raising their children. He added that male applicants were already on their list.

Senator Buford made a motion to approve the Scholar House project. The motion was seconded by Representative Wayne and passed by unanimous roll call vote.

Representative Denham asked John Hicks, Deputy Budget Director, (GOPM), and Jim Abbott, Commissioner, Department for Facilities and Support Services, to present the monthly project report submitted by the Finance and Administration Cabinet. Mr. Hicks first reported a scope increase of $2.2 million for the Kentucky Community and Technical College System (KCTCS) to construct a 12,000 square foot research wing for the Emerging Technology Center at the West Kentucky Community and Technical College (WKCTC) in Paducah.

Mr. Hicks said the 2006-08 Executive Budget appropriated $16,518,000 in bond funds to construct an emerging technology center at WKCTC, which is currently being designed. The additional research wing would be funded from two sources: $1 million in restricted funds from the University of Kentucky (UK) and $1.2 million in private donations from WKCTC's foundation.

Mr. Hicks said since 1995, a partnership has existed between UK, WKCTC, and Murray State University to improve the number of engineering graduates in the Purchase region. UK has already committed $1 million to the project.

Representative Wayne asked if the private funds were in hand.

Gary Cloyd, Director of Facilities Management, KCTCS, and Dr. Barbara Veazey, President, WKCTC, joined Mr. Hicks at the table. Dr. Veazey said funds were in hand to make the transfer from the local foundation to KCTCS and the names of donors would be available. Representative Wayne asked Dr. Veazey to provide the Committee with those names.

Senator Tori asked when the new technology center would come on-line. Mr. Cloyd said it is scheduled for completion in August 2009. He added that they anticipate bidding the project including the research wing addition in February 2009.

Representative Damron made a motion to approve the scope increase. The motion was seconded by Representative Wayne and passed by unanimous roll call vote. The revised project scope is $18,718,000.

Mr. Hicks next reported an unbudgeted project for the Department of Military Affairs to construct two helipads and add 1,400 feet taxiway at Bluegrass Station in Lexington, Kentucky. The project scope is $1,498,000, and is 100% federally funded from the U.S. Department of Defense.

Representative Wayne asked when the need for this project was identified since it was not included in the Department of Military Affairs' 2008-2014 Capital Plan submitted in April 2007. Mr. Charles Flynn, Chief Administrative Officer, Department of Military Affairs, said the need for this project came about after the current lessee, Special Operations Forces Support Activity (SOFSA), submitted and modified the six-year plan. He added that if the federal government has discretionary money at the close of the federal fiscal year (September 30), those funds are often utilized by the states for projects.

Representative Wayne asked if there was a proven need in the capital plan for this project. Mr. Flynn explained that there are two helicopter hangars at this installation separated by an area that serves as the airport, taxiway, and helicopter landing site. This space between the two hangars needs to be filled in and the helipad extended so the incoming helicopters do not land too close to the existing hangar.

In response to another question from Representative Wayne, Mr. Flynn said to his knowledge this need did not exist when the Department of Military Affairs' capital plan was submitted.

Senator Tori said in view of the fact that Kentucky deploys more National Guard troops that any other state, these air strips are nice to have but perhaps were not considered a high priority when the agency submitted its six-year plan. She said this is a good project and not a waste of money.

Senator Buford said Bluegrass Station might attract more training facilities if the added space was there and that the 1,400 feet of new taxi runway is extremely important. The state has an opportunity to use available federal funds for facilities at Bluegrass Station, and this project will allow for a safer place for the men and women to train.

Senator Buford made a motion to approve the scope increase. The motion was seconded by Representative Damron. The motion passed. Seven members voted affirmatively and one member voted "No".

Representative Damron explained his "Yes" vote and said Bluegrass Station should maximize the use of available federal dollars.

Representative Wayne explained his "No" vote by saying this project was not only costing Kentucky taxpayers but it would also increase the public debt that is connected with the Iraq war.

Representative Denham next asked Nancy Brownlee, Director, Division of Real Properties, to discuss lease reports. Mr. Brownlee first reported a lease modification for the Cabinet for Health and Family Services (CHFS) (PR-2829) in Montgomery County. The modification provides for an increase of 3,409 square feet (SF) for additional staff and programmatic needs. The staff is currently split between the first and second floors and this expansion offered an opportunity to consolidate the using agency onto a single floor, provide for additional space requirements, and accomplish the Boni Bill security measures for the office.

Ms. Brownlee said it is anticipated that the renovation work to this building would be completed four to six months after the county awards the bid for the project. Ms. Brownlee said the square footage will change from 6,493 to 9,902 and the annual rent will change from $87,656 to $133,677. Ms. Brownlee said this modification was being reported because the proposed modification increases the annual rent to above $100,000, the threshold for reporting.

Representative Wayne said he was encouraged by the Boni Bill modifications and asked how they were going in comparison to modifications of the other offices. Ms. Brownlee said three large requests had been received listing numerous improvements due to the security of those facilities. A staff member assigned to implement the Boni Bill improvements has gathered the necessary bids for each of the leased spaces and is continuing to complete the process in a timely manner.

Representative Damron said this lease was different in that the Montgomery County Fiscal Court (a political subdivision) is actually the lessor. He asked Ms. Brownlee if any preference or encouragement was given to local governments when securing leased space. Ms. Brownlee responded affirmatively and said state-owned space is considered first, and if none is available, then space in local governmental buildings is considered. If neither of the two types of space is available, the state advertises for space.

Representative Damron questioned whether it would be appropriate for county governments to construct a building, lease it to the state, and at the end of twenty years transfer ownership to the state. He asked if there was anything in the statutes that would give the incentive to do this. Mr. Brownlee said she was not sure if there was anything in state laws, but Real Properties can approach other governmental agencies about leasing space without the advertising requirements.

Representative Damron said the cost of capital for the government to construct a building is dramatically less than the cost of capital for a private investor. He said if the state does not offer any incentive for other government agencies to build and lease, then the leasing statutes may need to be changed to provide incentives to local governments to build.

Representative Wayne made a motion to approve the lease modification. The motion was seconded by Senator Tori and passed by unanimous roll call vote.

Representative Denham noted that a previously submitted lease modification report for the Environmental and Public Protection Cabinet (PR-3882) in Franklin County, was withdrawn until the December meeting.

The next lease modification report was for the Education Cabinet, Department for Workforce Investment, Office of Vocational Rehabilitation (PR-3920) in Franklin County. Ms. Brownlee said during efforts to renew the lease, the property owner advised they would require a rate increase. The lessor later agreed to renew at the existing terms and conditions for a five-year period provided that the square footage occupied by the using agency was corrected effective July 1, 2007. The proposed modification corrects the square footage by 6,590 SF from 17,066 SF to 23,656 SF. The annual cost of the leased space increases by $51,343 from $134,821 to $186,164 and the new expiration date is June 20, 2012.

Ms. Brownlee said the square footage was previously reduced when the agency vacated the fourth floor of the building. At the time, the mechanical and lobby areas of the building were erroneously removed from the leased amount of space. Ms. Brownlee apologized to the Committee for the timing of reporting this item. In order to correct the rentable square footage, the plans for this building were redrawn prior to the final approved plans with both the previous redraws resulting in a modification of space just under $50,000 a year. However, the modification's actual cost was $51,343 and should have been reported prior to execution to the lease modification. However, due to the sequence of events that led up to the modification including the redraws and an extended illness by a staff member, Real Properties made an honest administrative mistake in reporting after the fact. No action was required by the Committee.

Ms. Brownlee next discussed two modifications for improvements associated with leased facilities. The first modification was for the Department of Parks Sign Shop (PR-1164) in Franklin County. The Department of Parks submitted a request for additional electrical circuits and outlets at a cost $4,560. The cost of the modifications will be amortized over the remaining lease term (June 30, 2010). The second modification was for the CHFS, Department for Community Based Services (PR-4460) in Pulaski County. CHFS submitted a request to convert two smoking areas to office areas at a cost of $5,350. The cost of the modification will be amortized over the remaining lease term (June 20, 2008). No action is required by the Committee.

The last report Ms. Brownlee discussed was a report of leases with square footage modifications for the period of July through September 2007. The six lease modifications reflect a net increase of 7,460 SF in the amount of leased office space and an increase of $61,327 in annual rental costs. No action is required by the Committee.

Representative Denham next welcomed Sandy Williams, Financial Analyst, Kentucky Infrastructure Authority (KIA). Ms. Williams presented four KIA Fund A

(Federally-Assisted Wastewater Revolving Loan Fund) loan for the Committee's approval. The first loan was for $191,441 for the City of Alexandria in Campbell County. The funds will be used to assist in funding a $316,441 project to install sewer lines to 44 homes in a subdivision.

Representative Denham asked Ms. Williams if KIA will apply the standard by which the City of Alexandria was given a hardship rate to all applicants. Ms. Williams responded affirmatively.

Representative Damron asked how KIA determines the rates it sets for its loans. Ms. Williams said the regulation that governs both Fund A and Fund F loans outlines how the standard and non-standard (hardship) rates will be applied. She said there are certain criteria KIA uses, including the median household income and who benefits from the project.

In response to comments from Representative Damron, Ms. Williams said for projects that affect a city's entire water system, such as a treatment plant upgrade, KIA applies the median household income of the jurisdiction, either the city or county. For projects that effect only portions of the water system, KIA will base the rate on individual census tract information for that district. Referring to a KIA loan for Jessamine County that was later on the Committee's agenda, Ms. Williams said the manager of the Nicholasville system provided the individual census tract information for this specific project, and based upon a weighted average of those census tracts, it was still was over the state median household income, which means KIA offered the standard loan rate for the Jessamine County project.

Representative Damron asked if the Jessamine County project received the standard rate rather than the hardship rate because some high income areas of the county had been annexed into the city district. Ms. Williams explained that the weighted average median household income for the project's service area was greater than the median household income of the state. She said this is the first project the City of Nicholasville has sent to KIA since KIA's regulation changed in October that permitted individual census tract information to be submitted.

Representative Wayne asked Ms. Williams if any of the Fund A loans had been bid, and asked if KIA had changed its prior policy of having project bids before they are brought to the Committee. Ms. Williams said at its October KIA meeting, the board did allow KIA staff to offer loan commitments to borrowers prior to the project receiving bids.

Representative Wayne said historically the Committee reviews KIA projects after the project bids are in place. He then asked Ms. Williams to explain the logic behind this procedural change and if KIA plans to submit revised projects should the bid exceed the loan amount. Ms. Williams said if the loan amount has to be adjusted, then that increase in the loan amount would be brought back to this Committee for approval prior to release of any construction funds. As to the logic of the new procedure, Ms. Williams said KIA has revised the process based on feedback from several larger potential borrowers. She explained that larger borrowers do not want to use available funds from KIA for their projects because KIA cannot commit to them early in the process that funds would be available. KIA has tried to revise the process to allow them to get a conditional commitment of funding. Applicants still must complete all of the same steps.

Representative Wayne said he objected to this change and in his opinion the proper sequence was to have the bids in place and then bring the project before the Committee. He said he did not understand the reasons for the change, unless someone is benefitting from this that he was not aware of. Ms. Williams said KIA was reverting to a policy that was in place with the beginning of the program in 1988. This was the process and it was changed in early to mid 1990s at the request of the KIA Board members who did not want to see projects more than once.

In response to questions from Representative Wayne, Ms. Williams said in the past, the board reviewed the initial loan request with estimated construction amounts. Once the project was bid, if bids came in over budget, KIA staff would have to take the project back before the board for approval again. She said to reduce the number of times that this information had to be taken before the board, board members requested in the mid-1990's that the loan be presented once, that is after the project was bid.

Representative Wayne said he thought the reversion to the 1998 methodology was bad policy.

Senator Tori made a motion to approve the Fund A loan. The motion was seconded by Senator Rhoads and passed by roll call vote. Six members voted affirmatively and two members passed.

Representative Damron explained his "Pass" vote. He said there were real concerns about KIA's new procedures for determining interest rates and presenting loan commitments to the Committee prior to receiving construction bids for the project.

Representative Wayne explained his "Yes" vote. He said he was not going to vote against the project, but he objected to the process and hoped Ms. Williams would carry this message back to the KIA board members. He said the previous policies were much better.

Representative Denham said he thought it would be appropriate for KIA to draft a letter to the Committee in regard to the concerns and issues that had been raised during today's meeting.

Ms. Williams then presented a $1,469,778 Fund A loan for the City of Murray in Calloway County. This loan will be the single source of funding for this project, and will be used for construction of sewer lines to annexed subdivision households. The non-standard interest rate is 1.0% for a 20-year term.

Representative Denham noted that this project has not yet been bid and would proceed in the same manner as the previous Fund A loan.

Senator Rhoads made a motion to approve the Fund A loan for the City of Murray. The motion was seconded by Senator Tori and passed by roll call vote. Six members voted affirmatively and two members passed.

The third loan Ms. Williams presented was a Fund A loan for $54,690,822 for the City of Richmond in Madison County. This is the largest Fund A loan in KIA's history. The funds will be used to assist in funding a $57,843,022 project to construct a wastewater treatment plant. The loan will have a 20-year term at a non-standard interest rate of 1.0%.

Representative Rudy made a motion to approve the Fund A loan for the City of Richmond. The motion was seconded by Senator Tori and passed by roll call vote. Six members voted affirmatively and two members passed.

The fourth loan was for $1,465,487 for the Regional Water Resource Agency in Daviess County. The funds will be used to assist in funding a $1,709,375 project to extend sewer service to the Glenview Subdivision and to undertake sewer upgrades throughout the City of Owensboro. The non-standard interest rate is 1.0% for a 20-year term.

In response to a question from Senator Buford, Ms. Williams responded that there are five different sub-projects combined within this project. Four of the projects have been bid and one has not.

Representative Damron asked Ms. Williams if the residents in this specific subdivision pay a different rate than the residents of the rest of the community. Ms. Williams responded that they do not.

Senator Rhoads made a motion to approve the Fund A loan for the Regional Water Resource Agency. The motion was seconded by Senator Tori and passed by roll call vote. Six members voted affirmatively and two members passed.

Ms. Williams next reported five KIA Fund B (Infrastructure Revolving Fund) loans for the Committee's approval. The first loan was for $50,000 for the City of Burgin in Mercer County. The funds will be used to construct a water lines and a water main. The interest rate is the standard rate of 2.7% for a ten year term.

The second loan presented was for Hopkinsville Electric and Energy Net in Christian County in the amount of $3,000,000 to construct a fiber optic cable from Hopkinsville to Bowling Green. The loan will have a ten year term at the non-standard rate of 0.7%.

In response to a question from Senator Rhoads, Ms. Williams said KIA has the statutory authority to make infrastructure loans for water, sewer, electric, broadband.

Representative Denham noted that none of the Fund B loans had been bid.

Senator Tori made a motion to approve the Fund B loan for the Hopkinsville Electric and Energy Net. The motion was seconded by Senator Rhoads and passed by roll call vote. Six members voted affirmatively and two members passed.

The next Fund B loan presented was for the Marion County Water District in the amount of $340,000. The funds will be combined with a line item grant in the amount of $410,000 for a total project scope of $750,000, and will be used to construct a water storage tank in the southeast portion of Marion County. The loan will have a 20-year term at the non-standard rate of 0.7%.

The next Fund B loan presented was for the City of Williamsburg in Whitley County in the amount of $400,000 to make improvements to a water treatment plant. The funds will be combined with other funding for a total project amount of $3,237,440. The loan will have a 20-year term at a non-standard rate of 0.7%.

The last Fund B loan Ms. Williams presented was for the Logan-Todd Regional Water Commission in the amount of $400,000. The funds will be combined with other funding for a total project amount of $1,500,000, and will be used to upgrade membrane filters at the Logan-Todd Regional Water Treatment Plant. The loan will have a ten year term at the non-standard rate of 0.7%.

Senator Rhoads made a motion to approve the Fund B loans. The motion was seconded by Representative Wayne and passed by roll call vote. Six members voted affirmatively and two members passed.

Ms. Williams next presented two KIA Fund C (the Governmental Agencies Loan Fund) loans for the Southeast Daviess County Water District ($1,014,995) and the West Daviess County Water District ($1,173,708) to assist with construction of a water tank. Both loans have a standard interest rate of 3% and a term of five years.

Representative Denham noted that these two projects have been bid. Ms. Williams said that was also her understanding.

Representative Wayne made a motion to approve the Fund C loans. The motion was seconded by Senator Rhoads and passed by unanimous roll call vote.

Next Ms. Williams reported five Fund F (Federally Assisted Drinking Water Revolving Loan Fund) loans. The first loan was for the City of Richmond in Madison County in the amount of $4,000,000. The loan will be used to construct a new raw water intake and pump station to increase the plant's capacity from eight to twelve million gallons a day. These funds will be combined with other project financing for a total project scope of $7,108,951. The loan will have a 20-year term and a non-standard 1.0% interest rate.

The second Fund F loan was for the Letcher County Water and Sewer District in the amount of $781,000. The loan will be used to extend water service to residents in the Little Cowan area. These funds will be combined with line items grants for a total project scope of $1,193,000. The loan will have a 20-year term and a non-standard 1.0% interest rate.

Ms. Williams reported a Fund F loan for the Madison County Utility District for $1,004,560. The loan will be used to assist with water system improvement projects. These funds will be combined with other project financing for a total project scope of $1,504,560. The loan will have a 20-year term and a non-standard 1.0% interest rate.

Ms. Williams presented a loan for the Breathitt County Water District in the amount of $1,261,000. The loan will be used to extend water service in Southern Breathitt County. These funds will be combined with other project financing for a total project scope of $2,295,000. The loan will have a 20-year term and a non-standard 1.0% interest rate.

The last Fund F loan was for the City of Nicholasville in Jessamine County for $8,000,000. The loan will be used for renovations to the water treatment plant. These funds will be combined with other project financing for a total project scope of $13,090,400. The loan will have a 20-year term and a standard 3.0% interest rate.

In regards to the Breathitt County project, Senator Rhoads asked what would happen if the project is not approved today. Ms. Williams responded that if the loan was not approved then the conditional commitment of funding will be rescinded and the project will not move forward.

Senator Buford asked if KIA, when approving these projects, considered the current water supply debate between the Kentucky American proposal to build a new treatment plant versus a water pipeline coming from the Louisville Water Company. He questioned whether it would be wise to wait six months on some of these projects until a decision has been made regarding the water supply for Central Kentucky.

Ms. Williams said the KIA board did not address that particular issue with regard to any of these projects.

Senator Buford said Kentucky American is considering running its own line through Owen County and into the river. If they do this, it is unlikely that the City of Lexington would ever be able to buy water from them if it became for sale. It would be unaffordable, as it would be tied to the other counties supplying treated water. The other counties want to own a partnership in that which makes it even more difficult. If it comes from the river through the Louisville Water Company, it would seem that building small water treatment plant purification programs might not be in the best interest of the rate payers.

Senator Tori made a motion to approve the Fund F loans for the City of Richmond, the Letcher County Water and Sewer District, and the Breathitt County Water District. The motion was seconded by Representative Wayne and passed by unanimous roll call vote.

Senator Rhoads made a motion to approve the Fund F loans for the City of Nicholasville and the Madison County Utilities District. The motion was seconded by Representative Wayne and passed by roll call vote. Six members voted affirmatively and two members passed.

Representative Denham asked Ms. Williams if she understood the issues and concerns that were discussed during the meeting. He said it was important that KIA address these issues for everyone's benefit. He asked her to relay the Committee's concerns to the board and added that staff would welcome any correspondence from them.

Ms. Williams next reported various coal/tobacco development grants that were funded through line-item appropriations from the General Assembly in 2004 and 2006. Representative Denham said these grants did not require Committee action.

Representative Denham next invited Tom Howard, Executive Director, Office of Financial Management (OFM), Jim Host, Chairman, Louisville Arena Authority (Authority), and Tom Rousakis, Vice President, Goldman Sachs to discuss a new bond issue, Kentucky Economic Development Finance Authority (KEDFA) Louisville Arena Project Revenue Bonds, Series 2007A and Taxable Series 2007B (Louisville Arena Authority, Inc.).

Mr. Host said the Authority has completed its analysis of the new Louisville Arena project, and has gone through KEDFA for approval of conduit bonds in the amount of $354 million. He said the Authority has already locked in with the Mortenson Company, the design build firm, for an initial guaranteed maximum price of $254 million for construction of the facility. This figure also includes a 15% contingency. There will also be a second guaranteed maximum price that will be established by the middle of January to the end of January which will carry a 6% contingency. The final guaranteed maximum price, which will be due the end of May, will have a 2% contingency.

Mr. Host said the project has multiple funding streams including Louisville/Jefferson County Metro Government (Metro) contributions; state tax increment financing (TIF) revenues; and category A revenues, which are contractually obligated revenues such as external and internal advertising revenues and annual sponsorship revenues; and category B revenues, which are from ticket sales, concessions, and catering.

Mr. Host said the Authority has 15 Board members who have served on this project as unpaid volunteers, and not a single staff person has been paid. All work has been done as a public service by volunteers who are hopefully about to see the fruits of their labor.

Mr. Host said the Authority has instituted a training program, the first ever in Louisville, to train minorities to be electricians and carpenters. When implemented, participants in the program will account for 75% of the project work force. Most participants will be from Kentucky and southern Indiana. Twenty-two percent of the people on the project will be minorities in accordance with the request for proposals.

Representative Denham asked if the Louisville Arena Authority has received its underlying ratings yet. Mr. Host set he met with bond counsel and the representatives of the rating agencies two weeks ago for their final deliberations. He said they expect to have their ratings before or after Thanksgiving.

Representative Denham noted the cost of the bond insurance is $11,388,000. He asked if this amount is in line with a project of this scope. Mr. Rousakis said the underlying ratings are expected to be in the BBB range for this type of transaction. As such, the bond insurer, Ambac Inc., will be taking a significant amount of risk and so the insurance cost reflects that risk. Mr. Rousakis said a competitive process was used to procure bond insurance to get the best price for the level of risk, and the cost is very much in line for projects of this type.

Representative Denham asked Mr. Rousakis to describe the risk being undertaken with this bond issue. Mr. Rousakis explained that the bond transaction is shifting the project's risk to investors. And the risk the investor takes is the risk that sufficient revenues are generated to pay the debt service on the bonds over time. In this case, investors will be taking the risk that this project gets done on time and on budget, that when it opens the University of Louisville continues selling out all of its games, and that the revenues from the arena continue to be generated as projected. The bonds have the benefit of a guarantee from Louisville Metro Government which is a very solid source of payment within this bond indenture. Then there is the risk of the TIF revenues that are dependent upon the growth in the designated district in downtown Louisville.

In response to comments from Representative Denham, Mr. Rousakis agreed that the concern investors and the rating agencies have is the revenue stream could possibly or not possibly be generated from this project.

Representative Wayne thanked the individuals for the good work they were doing on the arena project. He said he realized this has been a long process and a lot of people have invested a lot of time, effort, creativity and energy into this. He then asked if the bond rating is not BBB what will happen. Mr. Rousakis said if the bonds are not rated BBB one option would be to continue to work on the structure of the transaction to get to the BBB range, based on the needs of the insurers and the rating agencies. He said he was confident that they will get there based on the feedback they have gotten at this point in time. If they cannot get the BBB rating, he said they could sell a portion of the bonds as un-insured. Mr. Host added that the Authority had the exact same question as the committee. He assured the Committee that the bond issue will move forward because it has been put together the right way.

Representative Wayne asked what weight did the rating agencies give the (TIF) revenues in the rating process. He said it was his understanding the TIF financing agreements for the arena have not been finalized. Mr. Rousakis responded that they are still waiting to hear the results of the analysis on the state's portion of the revenue stream. He explained that this project is a little bit unusual from what they have seen in other types of TIF projects, so they are doing everything they can to market this portion of the transaction to help the rating agencies understand what its strengths are.

Representative Wayne noted that the basis points and the insurance associated with this project were much higher than normal. He said this sounds like a high risk. He said he did not know anything about the bond insurer, Ambac, and requested more information about the company. Mr. Rousakis said Ambac is one of the major bond insurers in the market. Ambac's AAA rating is passed on to the bond issue because Ambac ensures the timely payment of principal and interest. What they do is insure bonds that offer a AAA rating to investors to insure the timely payment of principle and interest. Ambac is NBAIA certified. He explained the Authority gave notice to bond insurers of the proposed transaction and solicited bids on the transaction. He said three of the five bidders expressed a willingness to insure these bonds if the bonds are rated at least BBB. Of those bids, the Ambac bid was the most competitive and the Authority has been working with Ambac over the last three to four months on tightening up all the agreements, such that Ambac is satisfied at the end of the day that they are going to have the best security. He said the insurers are really the investor at the end of the day if they are going to put their premium behind the bond.

In response to a question from Representative Denham, Mr. Host said the tax increment finance agreements have been finalized and signed by the Secretary of the Finance Cabinet. He said he has not signed it yet.

Senator Tori asked about the status of the sale of naming rights on the arena. Mr. Host said they have hired Lurfield Team Services through a competitive process. He said in the Authority's estimates the firm projects generating $40 million dollars over a 20-year period of time, but the Authority believes it can get $50 million. He said he anticipated that the sale of the naming rights should be completed within the next six to nine months.

Representative Damron thanked Mr. Host for appearing before the Committee. He then asked if Ambac will be responsible for insuring the entire $360 million bond issue. Mr. Rousakis responded that Ambac will be liable for the entire amount, assuming the bonds receive investment grade ratings.

In response to another question from Representative Damron, Mr. Rousakis said the bond insurance and the basis points are in the appropriate range for this type of project financing arrangement.

Representative Damron asked why the Authority choose not to work with a financial advisor on this transaction. Mr. Host said he served as the volunteer financial advisor through the entire project.

Representative Damron noted that the Metro government has made a commitment for an additional $99 million dollars, a 50% increase on what they are already committed to. He asked what will trigger that additional payment for them. Mr. Host said if revenues are insufficient to meet the Authority's obligations, the Authority would do the following: tap the TIF reserve fund, which is calculated as 35% of debt service; tap $3 million from their renovation fund, or tap 55% of available funds that are left. And if there is no money left after they do all of that, the Authority would then use the additional funds the Metro government has committed.

Mr. Host said they feel confident that there will be sufficient revenues such that 55% will go back to the project and 45% will go back to the city to pay back the Metro Minimum on an annualized basis. He said a cash reserve will be built into the flow of funds. He said they established the benchmark for the TIF in 2005.

Representative Damron asked if the interest is being capitalized for five years to get around the rating agencies concerns. Mr. Rousakis said they are capitalizing interest only through project completion with a little bit of cushion in case there is a delay in the opening of the project. He added that the TIF money does not flow from the local and state governments until the project is complete.

Representative Damron asked what is the true interest cost on this bond issue. Mr. Host responded that it is 5.52%, which includes all the premiums, all of the cost of issuance, and everything else.

In response to another question from Representative Damron, Mr. Host said he would be glad to appear before the Committee once the transaction is complete and make a progress report. He added that this bond issue is not a general obligation of the state, which is why Ambac has to be involved. It is not a general obligation of the city. Therefore, it's the first issue that is structured this way. It is essentially being done like a revenue bond issue without any guarantees behind anything, which is why the bond insurance is needed in order to get to the needed bond rating.

Representative Damron noted that the state utilizes bond insurance from time to time, but at a lower rate. Mr. Host explained that was because the state's credit is pledged. Mr. Rousakis added that the second best bid for bond insurance was 190 basis points, compared to Ambac's bid that was 150 basis points.

Representative Denham said Representative Damron's comment is in order and the Committee would welcome an update.

Senator Buford asked if these two bidders gave any indication that they were concerned that the bond issue might not be a BBB. Mr. Rousakis said the way the Authority structured the issue, it was necessary only to get a BBB rating.

In response to another question from Senator Buford, Mr. Host said they did have difficulty in getting people to understand the state's method of TIF financing because it is different. He added that the participants understand it a whole lot better now than they did beforehand.

Mr. Host said that it is difficult to get an insurer like Ambac to insure these bonds. He said he had been involved in a lot of businesses and it is the toughest thing he had ever done.

Senator Buford asked if the Metropolitan Sewer District issued bonds to fund the floodwall yet. Mr. Host said there is no need for bonds for the floodwall because the arena's foundation will function as the floodwall. He explained that they moved the elevation of the floor up to where it is above the 100-year flood plain. He said $6 million was saved by doing this. There will be parking underneath the facility down to the water table.

Representative Denham asked what the schedule was for issuance of the bonds and construction of the project. Mr. Host said they will have a better idea of where they are in the middle of December. He said it was agreed this morning to recommend to the Authority at its next meeting in December to move forward in terms of the bond issue. He said that strategy may be negated by how the credit markets are at that time. He said as far as construction, they will begin demolition of some parts of the property in March 2008. The Request for Proposals for demolition will be put out November 26, and construction will start in August 2009 and take 26 months. He said they anticipate completion of the project in September or October 2010, and opening in November 2010. Mr. Host said the Louisville Gas & Electric Plant, which is being moved off of the site at a cost of $63.1 million, is on budget and ahead of schedule. So the schedule is firm.

Senator Seum made a motion to approve the Louisville Arena Authority bond issue. The motion was seconded by Senator Tori and passed by unanimous roll call vote.

Representative Denham said he appreciated the Authority's hard work and congratulated them for the effort.

The next report was given by Mr. Howard, Executive Director, and Terri Fugate, Deputy Executive Director, OFM; and Rick McQuady, Interim Chief Financial Officer, Kentucky Housing Corporation. The first new bond issue was Kentucky Housing Corporation (KHC) Single Family Housing Revenue Bonds, Series 2008 A, B, C and D, $100,000,000. The proceeds will be issued in one or more tax plans and one or more series, and will provide mortgage financing for low and moderate income home buyers.

Senator Tori made a motion to approve the KHC bond issue. The motion was seconded by Representative Rudy and passed by unanimous roll call vote.

The next new bond issue was KHC Revenue Bonds, Series 2007 (City Wide Housing project), $11,000,000. This conduit multi-family issue will fund a city-wide housing project in the city of Newport. The proceeds will provide conduit financing for the construction and rehabilitation of low-income housing around the City of Newport. Mr. Howard said this is a tax-exempt construction loan that is expected to be retired in two years with HOPE-VI and other funds.

Senator Buford made a motion to approve the KHC bond issue. The motion was seconded by Senator Rhoads and passed by unanimous roll call vote.

Ms. Fugate reported that the Kentucky Asset/Liability Commission (ALCo) approved a third amendment to an indenture for the 2005 General Fund Second Series Project Notes. This amendment will increase the size of the Project Notes Program from $950 million to $1.4 billion. She referred to a list of General Fund supported projects included in the Committee folders saying those projects will be eligible to receive interim financing under the Project Notes Program. She said these projects were approved by the 2005 and the 2006 General Assembly. Also recently added to the list to receive interim financing is the Energy Projects Economic Development Bond Pool for $100 million dollars which was approved in the 2007 Special Session, House Bill 1.

Senator Buford made a motion to approve the ALCo amendment. The motion was seconded by Senator Rhoads and passed by unanimous roll call vote.

The last report Ms. Fugate presented was the semi-annual report of the Kentucky Asset/Liability Commission. She said OFM is statutorily required to issue a report every six months on ALCo and its activities.

Mr. Howard noted that on Monday, November 5, 2007, the Supreme Court held oral arguments in Kentucky v. Davis, relating to the taxation of municipal bonds. He said the arguments went very well, and while no one can ever predict what the Supreme Court will do, a ruling in support of the state's position is anticipated sometime in February or March 2008.

Representative Denham asked if the bond ratings for Kentucky had improved in the last few months. Mr. Howard responded that early last year Standard & Poor raised the state's outlook from stable to positive and Moody's raised it from negative to stable. Kentucky's appropriation-supported credits are rated A+ by S&P, AA- by Fitch with stable outlook, and Aa 3 stable by Moody's. The state's "issuer" credit rating, or what would be the state's general obligation rating if the state issued general obligation bonds is a notch higher, or Aa 2 by Moody's and AA- by S&P. Fitch does not give issuer credit ratings to states that do not issue general obligation debt.

Mr. Howard said the rating agencies look at trends in finances, the fact that the state economy has stabilized, and the timely adoption of the current budget.

Representative Denham asked how interest rates have affected the state's cash flow and asset liability management. Mr. Howard said the state has refinanced as many outstanding bonds as possible, and recent declines in interest rates have affected the Treasury bond market rather than the municipal bond markets, where the rates have not changed much. He said rates have been volatile.

Representative Damron said as they prepare for the 2008 session, it is important to be mindful of the fact that rating agencies take into consideration whether or not the legislature is able to pass a budget. He said everything else is secondary when it comes down to the fact of being able to do the prudent thing and enacting a budget that generates enough revenues to balance the appropriations.

Mr. Howard responded that people will continue to read about structural balance within the budget. Even though revenues and expenditures may be equal in the budget, the rating agencies are looking for revenues and expenditures to be equal on a recurring basis.

Ms. Fugate then presented 12 new school bond issues with School Facilities Construction Commission (SFCC) debt service participation: Bardstown Independent (Nelson County), Bellevue Independent (Campbell County), Breckinridge County, Fleming County, Ft. Thomas Independent (Campbell County), Graves County, Kenton County, Larue County, Lawrence County, Martin County, Mayfield Independent (Graves County), and West Point Independent (Hardin County).

Senator Buford made a motion to approve the school bond issues. The motion was seconded by Representative Rudy and passed by unanimous roll call vote. Representative Damron explained his "Yes" vote. He said even though his firm handled nine of the twelve bond issues, he does not work in that section of the agency.

Next Ms. Osborne reported four locally-funded school bond issues submitted to the Committee for review this month: Breckinridge County, Hopkins County, Kenton County, and Monticello Independent (Wayne County). She said all disclosure information has been filed, and no further action is required on the bond issues.

Ms. Osborne said the Committee's next meeting is schedule for December 20 at 1:00 p.m. in the auditorium at the renovated State Office Building.